

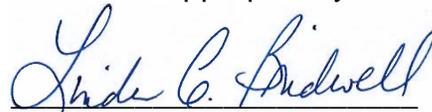
COMMONWEALTH OF KENTUCKY  
BEFORE THE PUBLIC SERVICE COMMISSION

In the Matter of:

ELECTRONIC APPLICATION OF BUFFALO	)	
TRAIL WATER ASSOCIATION, INC. FOR A	)	CASE NO.
RATE ADJUSTMENT PURSUANT TO 807	)	2021-00205
KAR 5:076	)	

NOTICE OF FILING OF COMMISSION STAFF REPORT

Notice is hereby given that, in accordance with the Commission's Order of May 24, 2021, the attached report containing the findings of Commission Staff (Staff) regarding the Applicant's proposed rate adjustment has been filed in the record of the above-styled proceeding. Pursuant to the Commission's May 24, 2021 Order, Buffalo Trail Water Association (Buffalo Trail Water) is required to file written comments regarding the findings of Staff no later than 14 days from the date of this report. The Commission directs Buffalo Trail Water to the Commission's July 22, 2021 Order in Case No. 2020-00085<sup>1</sup> regarding filings with the Commission. Electronic documents shall be in portable document format (PDF), shall be searchable, and shall be appropriately bookmarked.



Linda C. Bridwell, PE  
Executive Director  
Public Service Commission  
P.O. Box 615  
Frankfort, KY 40602

DATED SEP 10 2021

cc: Parties of Record

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<sup>1</sup> Case No. 2020-00085, *Electronic Emergency Docket Related to the Novel Coronavirus COVID-19* (Ky. PSC July 22, 2021), Order (in which the Commission ordered that for case filings made on and after March 16, 2020, filers are NOT required to file the original physical copies of the filings required by 807 KAR 5:001, Section 8).

STAFF REPORT  
ON  
BUFFALO TRAIL WATER ASSOCIATION  
CASE NO. 2021-00205

Buffalo Trail Water Association (Buffalo Trail Water) is a water utility organized pursuant to KRS Chapter 273 that owns and operates a water distribution system through which it provides retail water service to approximately 1,571 residential customers and 7 commercial customers that reside in Bracken, Harrison, Mason, Nicolas, Pendleton, and Robertson counties, Kentucky.<sup>1</sup> On May 14, 2021, Buffalo Trail Water filed an application with the Commission requesting to adjust its water rates pursuant to 807 KAR 5:076. The application was filed pursuant to the Commission's Order in Case No. 2020-00147.<sup>2</sup> To ensure the orderly review of the application, the Commission established a procedural schedule by Order dated May 24, 2021. Staff issued its first round of formal discovery on June 9, 2021, and a second round of formal discovery on July 16, 2021. On July 29, 2021, Buffalo Trail Water filed a motion requesting an extension of the deadline to respond to Staff's Second Request for Information. The Commission, on its own motion, granted the extension on August 6, 2021, and revised the procedural schedule extending the due date of Staff's report to August 31, 2021. On August 26, 2021, the Commission again, on its own motion, revised the procedural schedule revising the due date for Staff's Report to September 14, 2021.

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<sup>1</sup> *Annual Report of Buffalo Trail Water Association to the Public Service Commission for the Calendar Year Ended December 31, 2020* (Annual Report) at 12 and 49.

<sup>2</sup> 2020-00147, *Electronic Purchased Water Adjustment Filing of Buffalo Trail Water Association, Inc.* (filed May 14, 2020) at 3, ordering paragraph 5.

The Commission notes that in its 2020 Annual Report, Buffalo Trail Water reported a water loss of 9.68 percent.<sup>3</sup> Commission regulation 807 KAR 5:066(6)(3) states that for rate making purposes a utility's water loss shall not exceed 15 percent of total water produced and purchased, excluding water consumed by a utility in its own operations. At a 9.68 percent water loss, the annual cost to Buffalo Trail Water is \$26,346.<sup>4</sup>

To comply with the requirements of 807 KAR 5:076, Section 9,<sup>5</sup> Buffalo Trail Water used the calendar year ended December 31, 2020, as the basis for its application. Using its pro forma test-year operations, Buffalo Trail Water determined that a revenue increase of \$34,186 or 4.66 percent over test-year normalized revenues of \$734,299 was warranted.<sup>6</sup> On August 10, 2021, Buffalo Trail Water filed an update to its revenue increase to correct an error in its calculations. Buffalo Trail Water determined that a revenue increase of \$45,646 or 6.22<sup>7</sup> percent over test-year normalized revenues from

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<sup>3</sup> Annual Report at 57.

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	<u>Purchased Water</u>	<u>Purchased Power</u>
Pro Forma Expenses	\$ 263,509	\$ 8,537
Times: Total Water loss	9.6842%	9.6842%
 Excess Water Loss Reductions	 <u>\$ 25,519</u>	 <u>\$ 827</u>
 Total		 <u><u>\$ 26,346</u></u>

<sup>5</sup> The reasonableness of the proposed rates shall be determined using a 12-month historical test period, adjusted for known and measureable changes, that coincides with the reporting period of the applicant's annual report for the immediate past year.

<sup>6</sup> Application, Revenue Requirements Calculation.

<sup>7</sup> Buffalo Trail Water's Response to Commission Staff's Second Request for Information (Staff's Second Request) (filed Aug. 10, 2021), Updated Revised Required Calculations, Item 9.

rates of \$734,299 is warranted as shown in the table below. Buffalo Trail Water failed to include in its revenue requirement calculation, test year depreciation and amortization, which resulted in an understatement in its requested revenue increase. Additionally Buffalo Trail Water added rather than subtracted Other Operating Revenue, Miscellaneous Service Revenue, and Interest Income from the Overall Revenue Requirement. The revised rates requested by Buffalo Trail Water would increase the residential monthly bill of a typical residential customer using 4,221 gallons per month<sup>8</sup> by \$2.35 from \$37.63<sup>9</sup> to \$39.98 or approximately 6.25 percent.<sup>10</sup>

	<u>Buffalo Trail Water Association</u>
Pro Forma Operating Expenses	\$ 624,601
Plus: Avg. Annual Principal and Interest Payments	57,303
Debt Coverage Requirement	<u>11,461</u>
Overall Revenue Requirement	693,365
Less: Other Operating Revenue	57,856
Miscellaneous Service Revenue	19,650
Interest Income	<u>9,074</u>
Revenue Required From Water Sales	779,945
Revenue from Sales at Present Rates	<u>(734,299)</u>
Required Revenue Increase	<u>45,646</u>
Percentage Increase	<u>6.22%</u>

To determine the reasonableness of the rates requested by Buffalo Trail Water, Staff performed a limited financial review of Buffalo Trail Water's test-year operations.

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<sup>8</sup> Application – billinganalysis.pdf at 6.

<sup>9</sup> First 1,000 gallons at \$15.44; Next 4,000 gallons at \$6.89 ((3,221/1000) x \$6.89) = \$22.19 + \$15.44 for a typical residential bill of \$37.63.

<sup>10</sup> Buffalo Trail Water's Response to Staff's Second Request, UpdatedCurrent\_ProposedRates.pdf.

The scope of Staff's review was limited to determining whether operations reported for the test year were representative of normal operations. Known and measurable<sup>11</sup> changes to test-year operations were identified and adjustments made when their effects were deemed material. Insignificant and immaterial discrepancies were not necessarily pursued or addressed.

Staff's findings are summarized in this report. William Foley reviewed the calculation of Buffalo Trail Water's Overall Revenue Requirement. Sam Reid and Liz Stefanski reviewed Buffalo Trail Water's reported revenues and rate design.

### SUMMARY OF FINDINGS

1. Overall Revenue Requirement and Required Revenue Increase. By applying the Debt Service Coverage (DSC) method, as generally accepted by the Commission, Staff found that Buffalo Trail Water's required revenue from rates is \$828,655 to meet the Overall Revenue Requirement of \$842,357, and that a \$94,437 revenue increase, or 12.86 percent, to pro forma present rate revenues is necessary to generate the Overall Revenue Requirement.

2. Monthly Water Service Rates. Based upon the revised revenue requirement, Buffalo Trail Water proposed to increase all of its monthly retail water service rates evenly across the board by approximately 6.22 percent. Buffalo Trail Water did not

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<sup>11</sup> Commission regulation 807 KAR 5:076, Section 9 sets the standard for the determination of the reasonableness of proposed rates and states, in pertinent part, that the test period shall be "adjusted for known and measurable changes." See also Case No. 2001-00211, *The Application of Hardin County Water District No. 1 for (1) Issuance of Certificate of Public Convenience and Necessity; (2) Authorization to Borrow Funds and to Issue its Evidence of Indebtedness therefor; (3) Authority to Adjust Rates; and (4) Approval to Revise and Adjust Tariff* (Ky. PSC Mar. 1, 2002); Case No. 2002-00105, *Application of Northern Kentucky Water District for (A) an Adjustment of Rates; (B) a Certificate of Public Convenience and Necessity for Improvements to Water Facilities if Necessary; and (C) Issuance of Bonds* (Ky. PSC June 25, 2003); Case No. 2017-00417, *Electronic Proposed Adjustment of the Wholesale Water Service Rates of Lebanon Water Works* (Ky. PSC July 12, 2018).

performed a cost of service study (COSS). In response to Staff's First Request for Information (Staff's First Request), Buffalo Trail Water stated that it did not complete a COSS at this time, as there has not been any material change in the water system to warrant a COSS.<sup>12</sup>

The Commission has previously found that the allocation of a revenue adjustment evenly across the board to a utility's rate design is appropriate when there has been no evidence entered into the record demonstrating that this method is unreasonable and in the absence of a COSS. Finding no such evidence in this case, Staff followed the method proposed by Buffalo Trail Water and allocated the \$94,437 revenue increase across the board to Buffalo Trail Water's monthly retail and wholesale water service rates.

The rates set forth in the Appendix to this report are based upon the revenue requirement, as calculated by Staff, and will produce sufficient revenues from water sales to recover the \$828,655 Revenue Required from Water Sales, an approximate 12.86 percent increase. These rates will increase a typical residential customer's monthly water bill from \$37.63 to \$42.49, an increase of \$4.86 or approximately 12.91 percent.<sup>13</sup>

3. Nonrecurring Charges. Following the Commission's recent decisions,<sup>14</sup> Staff has reviewed Buffalo Trail Water's Nonrecurring Charges. The Commission found that as district personnel are currently paid during normal business hours, estimated labor

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<sup>12</sup> Buffalo Trail Water's Response to Staff's First Request (filed July 2, 2021), Item 10.

<sup>13</sup> The typical residential customer uses approximately 4,221 gallons per month.

<sup>14</sup> Case No. 2020-00141, *Electronic Application of Hyden-Leslie County Water District for an Alternative Rate Adjustment* (Ky. PSC Nov. 6, 2020), Case No. 2020-00167, *Electronic Application of Ohio County Water District for an Alternative Rate Adjustment* (Ky. PSC Dec. 3, 2020), Case No. 2020-00196, *Electronic Application of West Daviess County Water District for an Alternative Rate Adjustment* (Ky. PSC Dec. 30, 2020), and Case No. 2020-00195, *Electronic Application of Southeast Daviess County Water District for an Alternative Rate Adjustment* (Ky. PSC Dec. 30, 2020).

costs previously included in determining the amount of Nonrecurring Charges should be eliminated from the charges. In response to Staff's Second Request, Buffalo Trail Water provided updated cost justification information for the Nonrecurring Charges that are listed in its tariff.<sup>15</sup> Staff reviewed the cost justification information provided by Buffalo Trail Water and have adjusted these charges by removing Field Labor Costs and Office/Clerical Labor Costs.<sup>16</sup> Staff adjusted the mileage rate to the current allowable mileage rate by the Internal Revenue Service of \$0.56 per mile.<sup>17</sup> Such adjustments result in the following revised Nonrecurring Charges:

<u>Nonrecurring Charge</u>	<u>Normal Hours</u>
Meter Turn-On	\$16.80
Meter Test	74.80
Meter Re-Read	16.80
Service Call/Investigation	16.80
Service Reconnection	21.00
Returned Check Charge	9.00
Lock Removal	22.00
5/8 x 3/4 Inch Water Tap On	1,176.00

Buffalo Trail Water requested to remove from its tariff certain Nonrecurring Charges in its response to Staff's Second Request. Buffalo Trail Water's statement that the Meter Re-Setting Charge, the Service Line Inspection charge, and the Service Trip Field Collection charge no longer pertain to the utility and should be removed from its tariff.<sup>18</sup> Buffalo Trail Water is no longer providing these services, therefore, Staff agrees the charges should be removed from the tariff.

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<sup>15</sup> Buffalo Trail Water's Response to Staff's Second Request, Item 4.

<sup>16</sup> *Id.*

<sup>17</sup> <https://www.irs.gov/tax-professionals/standard-mileage-rates>.

<sup>18</sup> Buffalo Trail Water's Response to Staff's Second Request, Item 4.

The adjustments to the Nonrecurring Charges results in a decrease in Other Operating Revenue of \$2,438 as shown below.<sup>19</sup>

	Number of Occurrences	Utility Pro Forma	Adjustment	Pro Forma
Meter Turn-On Charge	11	\$ 440	\$ (255)	\$ 185
Meter Test Charge		-	-	-
Meter Re-Read Charge		-	-	-
Service Call/Investigation Charge		-	-	-
Service Reconnection charge	37	2,960	(2,183)	777
Returned Check Charge		-	-	-
Lock Removal Charge		-	-	-
Totals		\$ 3,400	\$ (2,438)	\$ 962

Buffalo Trail Water provided the Average Meter Connection Expense Cost Justification form for 5/8 X 3/4 Inch meter for the cost of a manual read meter as well as the cost of a radio read meter.<sup>20</sup> Buffalo Trail Water stated that the utility was upgrading from manual read meters to radio read meters and proposed to increase its meter connection fee by \$576 from \$600 to \$1,176, to reflect the current cost to install a meter.<sup>21</sup> Staff agrees that this proposed increase is reasonable to recover the increased cost to install a 5/8 X 3/4 Inch radio read meter.

#### PRO FORMA OPERATING STATEMENT

Buffalo Trail Water's Pro Forma Operating Statement for the test year ended December 31, 2020, as determined by Staff, appears below.

<sup>19</sup> *Id.*

<sup>20</sup> Buffalo Trail Water's Response to Staff's Second Request, Item 3.

<sup>21</sup> *Id.*

	Test Year	Adjustment	(Ref.)	Pro Forma
Operating Revenues				
Total Metered Sales	\$ 716,947	17,271	(A)	\$ 734,218
Other Water Revenues				
Misc. Service Revenues	28,724	(19,650)	(B)	
		(9,074)	(C)	-
Other Water Revenues	57,856	(2,438)	(D)	
		(50,790)	(E)	4,628
Total Operating Revenues	<u>\$ 803,527</u>	<u>(64,681)</u>		<u>\$ 738,846</u>
Operating Expenses				
Operation and Maintenance Expenses				
Salaries and Wages - Employees	148,284	(13,675)	(F)	
		(10,664)	(G)	
		(1,056)	(H)	
		(14,000)	(I)	108,889
Salaries and Wages - Officers		14,000	(I)	14,000
Employee Pensions and Benefits				-
Purchased Water	245,450	18,059	(J)	263,509
Purchased Power				-
Materials and Supplies	11,269	(14,756)	(F)	(3,487)
Contractual Services	155,193			155,193
Insurance	7,995			7,995
Commission Expense	1,403			1,403
Bad Debt	24,168			24,168
Miscellaneous Expense	30,838			30,838
Total Operation and Maintenance Expenses	624,600	(22,092)		602,508
Depreciation	176,712	(48,256)	(K)	
		669	(L)	129,125
Amortization	31,296			31,296
Taxes Other Than Income		10,664	(G)	10,664
Utility Operating Expenses	<u>832,608</u>	<u>(59,015)</u>		<u>773,593</u>
Utility Operating Income	(29,081)	(5,666)		(34,747)
Interest Income		9,074	(C)	9,074
Income Available to Service Debt	<u>(29,081)</u>	<u>3,408</u>		<u>(25,673)</u>

(A) Billing Analysis Adjustment. Buffalo Trail Water provided a billing analysis listing the water usage and water sales revenue for the 12-month test year in its

application. The total metered water sales revenue reported for the test year is \$716,947.<sup>22</sup> During the test year Buffalo Trail Water increased its service rates through a purchase water adjustment (PWA), due to an increase from its supplier.<sup>23</sup> In response to Staff's First Request, Buffalo Trail Water provided usage data,<sup>24</sup> which Staff used to calculate a normalized revenue amount based on the statistics compiled in the table below, which included the PWA increase. Subsequently, Staff increased test year water sales revenue by \$17,271 to reflect the increase in rates.

<u>Meter Size</u>	<u>Bills</u>	<u>Gallons</u>	<u>Revenue</u>
5/8 Inch	18,573	78,471,530	\$ 663,948
1 Inch	13	265,260	1,708
2 Inch	24	3,578,000	17,205
4 Inch	24	330,630	5,504
Mt. Olivet	12	1,374,000	35,710
Nicholas	12	3,191,000	<u>10,143</u>
Normalized Revenue			734,218
Test Year Revenues			<u>(716,947)</u>
Adjustment			<u>\$ 17,271</u>

(B) Water Tap Revenues. In the application, Buffalo Trail Water reported Miscellaneous Service Revenues of \$28,724,<sup>25</sup> which included \$19,650 in water tap revenues. In the test-year, Buffalo Trail Water installed 29 new meters. Tap-on fees are considered contributed capital, and it is not proper to recognize the collections of tap fees

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<sup>22</sup> Annual Report at 49.

<sup>23</sup> Case No. 2020-00147, *Electronic Purchased Water Adjustment Filing of Buffalo Trail Water Association, Inc.* (Ky. PSC May 14, 2020).

<sup>24</sup> Buffalo Trail Water's Response to Staff's First Request, Combined\_Statistics.xlsx

<sup>25</sup> Application, stmtadjustedoper.pdf. Updated files to First Data Request, Updated 2020 TB, (filed Aug. 11, 2021).

as revenue. Tap-on fees should be recorded in Account No. 215.2 - Donated Capital, a sub-account of unappropriated retained earnings. Therefore, Staff made a decrease to Miscellaneous Service Revenues.

(C) Interest Income. In the application, Buffalo Trail Water reported Miscellaneous Service Revenues of \$28,724;<sup>26</sup> this amount includes \$9,074 in Interest Income. Interest Income is not Operating Revenue and Staff reclassified it as an Other Income. Therefore, Staff reduced Miscellaneous Service Revenue by \$9,074 and increased Interest Income by \$9,074.

(D) Other Water Revenues–Nonrecurring Charges. As shown above, the adjustments to the Nonrecurring Charges results in a decrease in Other Operating Revenue of \$2,438.<sup>27</sup>

(E) Other Water Revenues. In the application, Buffalo Trail Water reported Other Water Revenue of \$57,856, which included Miscellaneous Income of \$51,480.<sup>28</sup> In response to Staff's First Request, the utility responded that \$50,790 of this amount was a reimbursement for relocating a water line for Robertson County School<sup>29</sup> Staff decreased Other Water Revenue by removing this amount as the revenue was a reimbursement and will not reoccur in the future.

(F) Expenses Related to Meter Installations. During the test year, Buffalo Trail Water installed 29 new water connections<sup>30</sup> but did not capitalize the expenses for the

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<sup>26</sup> *Id.*

<sup>27</sup> Buffalo Trail Water's Response to Staff's Second Request, Item 4.

<sup>28</sup> Buffalo Trail Water's Response to Staff's First Request, Item 11.

<sup>29</sup> *Id.*

<sup>30</sup> Buffalo Trail Water's Response to Staff's Second Request, Item 1.

tap installation. Buffalo Trail Water recorded Labor expense of \$13,675 and Materials Expense of \$14,756 to install the new water connections.<sup>31</sup> The Uniform System of Accounts for Class A/B Water Systems (USoA) requires that these costs be capitalized as Utility Plant in Service and depreciated over their estimated useful lives.<sup>32</sup> Buffalo Trail Water incorrectly reported these costs as test-year expenses. To correct this accounting error in pro forma operations, Staff removed the amount collected for these connections from test-year expenses and increased Depreciation expense. Therefore, Staff decreased Salaries and Wages-Employees by \$13,675, and Materials and Supplies by \$14,756 for a total adjustment of \$28,431. In addition, Staff has capitalized the costs and made a corresponding adjustment to test-year depreciation as shown in adjustment (L).

(G) Taxes Other Than Income-Reconciliation. In the application, Buffalo Trail Water reported \$0 to its Taxes other than Income.<sup>33</sup> However, on its annual report, Buffalo Trail Water included in Salaries and Wages general ledger account 60300 FICA/Medicare Tax Expense for \$9,457 and 60400 Unemployment Expenses for \$1,207.<sup>34</sup> Therefore, Staff made a reclassification adjustment from Salaries to increase Taxes Other than Income \$10,664.

(H) Employee Pensions and Benefits. In the application, Buffalo Trail Water reported \$0 in its Employee Pensions and Benefits expense.<sup>35</sup> However, during the test

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<sup>31</sup> *Id.*, Item 2

<sup>32</sup> USoA, Accounting Instruction 19 and 33.

<sup>33</sup> *Id.*

<sup>34</sup> Buffalo Trail Water's Response to Staff's First Request, Item 1a

<sup>35</sup> Application, Schedule of Adjusted Operations.

year Buffalo Trail Water paid \$4,800<sup>36</sup> to reimburse their only full time employee for the cost to provide their own health insurance. Buffalo Trail included in its General Ledger the reimbursement in Salaries and Wages. Staff spoke with the employee at Buffalo Trail Water about the allowance and was notified that Buffalo Trail Water pays for 100 percent of the employee's insurance plan. In addition, Buffalo Trail Water pays the employee \$900<sup>37</sup> annually for retirement investments. Staff notes that the Commission has consistently made ratemaking adjustments to reduce the cost of employer sponsored healthcare paid by some utilities when certain aspects of those benefit packages were found to be unreasonable based on a review of total salaries and fringe benefits. The Commission continues to place greater emphasis on evaluating employees' total compensation packages, including both salary and benefits programs, for market and geographic competitiveness to ensure the development of a fair, just and reasonable rate. The Commission has found that, in most cases, 100 percent of employer-funded health care does not meet those criteria.<sup>38</sup>

Consistent with precedent in which the Commission has reduced benefit expenses for utilities that pay 100 percent of an employee's health insurance coverage, Staff reduced Buffalo Trail Water's single health insurance premiums by 22 percent as shown in the calculation below.<sup>39</sup> Accordingly, Staff decreased Salaries and Wages by \$1,056.

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<sup>36</sup> Buffalo Trail Water's Response to Staff's First Request, Item 1.g.

<sup>37</sup> Supplement to First Request (filed Aug. 11, 2021), Item 1.g.

<sup>38</sup> Case 2020-00167, *Electronic Application of Ohio County Water District for an Alternative Rate Adjustment* (Ky. PSC Dec. 2, 2020). Case 2020-00296, *Electronic Application of Allen County Water District for an Alternative Rate Adjustment* (Ky. PSC Feb. 3, 2021).

<sup>39</sup> Bureau of Labor Statistics, Healthcare Benefits, March 2020, Table 3, private industry workers. (<https://www.bls.gov/news.release/pdf/ebs2.pdf>).

Type of Premium	Employer Contributions	Average Employee Contribution Rate	Monthly Premium Adjustment	Pro Forma Monthly Premium
Single Health Insurance	\$ 400	22%	\$ (88)	\$ 312
Total Pro Forma Monthly Premium				312
Times: 12 Months				<u>12</u>
Total Annual Pro Forma Premium				3,744
Less: Test Year				<u>(4,800)</u>
Adjustment				<u>\$ (1,056)</u>

(l) Salaries and Wages-Officers. In its test year, Buffalo Trail Water included the amounts paid to its officers in its Salaries and Wages-Employees expense.<sup>40</sup> Buffalo Trail Water responded to Staff's First Request with the board members' wages.<sup>41</sup> Buffalo Trail Water currently has six board members. Pursuant to KRS 273A.115 Section (2)(a), a water association may pay reasonable compensation to its board members for services rendered. Staff believes Buffalo Trail Water should be permitted to recover, for rate making purposes, the amount determined reasonable by the association and its members, who are the rate payers. Therefore, Staff reclassified \$14,000 from Salaries and Wages-Employees to Salaries and Wages-Officers as shown in the table below and verified with the general ledger.

<sup>40</sup> Application, Schedule of Adjusted Operations.

<sup>41</sup> Buffalo Trail Water's Response to Staff's First Request, Item 1.i.

<u>Commissioners</u>	<u>Test Year Salaries</u>
William L Clary	\$ 4,900
Randall Biddle	1,750
James D Curtis	1,900
Terry Cracraft	1,900
Aaron Myers	1,650
Clay Saunders	<u>1,900</u>
 Total	 \$ 14,000
Test Year Salaries	<u>-</u>
 Adjustment	 <u>\$ 14,000</u>

(J) Purchased Water. In its test year, Buffalo Trail Water reported a purchased water expense of \$245,450.<sup>42</sup> During the test year, Buffalo Trail Water filed and was approved for a PWA in Case No. 2020-00147. In order to annualize the purchased water, Staff calculated a Purchased Water expense using the new rate. This results in a purchased water expense of \$263,509. Therefore, Staff increased purchased water expense by \$18,059 in order to reconcile the test year amount with the reported purchased amount as shown below.

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<sup>42</sup> Application, Schedule of Adjusted Operations.

Purchased Water					
Period	Maysville		Western Fleming		Total
	Purchased	Dollars	Purchased	Dollars	
Jan-2020	448,000	\$ 0.00234	10,080,000	0.00214	\$ 22,620
Feb-2020	436,000	0.00234	8,699,000	0.00214	19,636
Mar-2020	407,000	0.00234	7,944,000	0.00214	17,953
Apr-2020	681,000	0.00234	8,624,000	0.00214	20,049
May-2020	564,000	0.00234	7,902,000	0.00214	18,230
Jun-2020	749,000	0.00234	10,438,000	0.00214	24,090
Jul-2020	701,000	0.00240	11,321,000	0.00214	25,909
Aug-2020	593,000	0.00240	12,419,000	0.00214	28,000
Sep-2020	721,000	0.00240	9,990,000	0.00214	23,109
Oct-2020	754,000	0.00240	9,457,000	0.00214	22,048
Nov-2020	516,000	0.00240	9,643,000	0.00214	21,874
Dec-2020	616,000	0.00240	8,651,000	0.00214	19,992
Purchased Water Expense					\$ 263,509
Test Year Purchased Water					<u>245,450</u>
Adjustment					<u>\$ 18,059</u>

(K) Depreciation Expense. In the application, Buffalo Trail Water reported its test year Depreciation Expense of \$176,712.<sup>43</sup> To evaluate the reasonableness of the depreciation practices of small water utilities, the Commission has historically relied upon the report published in 1979 by the National Association of Regulatory Utility Commissioners (NARUC) titled Depreciation Practices for Small Water Utilities (NARUC Study). When no evidence exists to support a specific life that is outside the NARUC ranges, the Commission has historically used the midpoint of the NARUC ranges to depreciate the utility plant. Upon examination, Staff found several assets not depreciated at the NARUC ranges midpoints. In this proceeding, Staff found no evidence to support depreciable lives that vary significantly from the midpoint of the NARUC ranges. After

<sup>43</sup> Application, Schedule of Adjusted Operations.

further review of Buffalo Trail Water’s plant ledger, Staff decreased Buffalo Trail’s Depreciation Expense by \$48,256 to \$128,456 as shown below.

<u>Asset Classes</u>	<u>Pro Forma Depreciation</u>
Source of Supply-Land	-
Structures & Improvements	\$ 617
Trans & Distribution Resv-Standpipe	4,816
Trans Dist Mains	116,159
Trans Dist Services	1,489
Utility Plant Meters	2,972
Trans Dist Hydrants	77
Trans Dist Other Equip	-
Office Equipment	833
Communication Equipment	-
New Office Building	<u>1,493</u>
Pro Forma Depreciation Expense	128,456
Less: Test Year Depreciation Expense	<u>(176,712)</u>
Depreciation Expense Adjustment	<u><u>\$ (48,256)</u></u>

(L) Capitalization of Test-Year Water Taps. As explained in adjustment (G) above, the expenses related to the installation of new water connections are capital expenditures that should be capitalized as Utility Plant in Service and depreciated over their estimated useful lives. Therefore, Staff calculated the annual depreciation amount for the test year and increased depreciation expense by \$669 as shown below.

Labor Expense Associated with Tap Ons	\$ 13,675
Materials and Supplies Expense Associated with Tap Ons	<u>14,756</u>
Test Year Tap On Expenses	28,431
Divided by: Useful Life of 42.5 Years	<u>42.50</u>
Pro Forma Depreciation Adjustment	<u><u>\$ 669</u></u>

OVERALL REVENUE REQUIREMENT AND REQUIRED REVENUE INCREASE

The Commission has historically applied a DSC method to calculate the Overall Revenue Requirement of water districts and water associations. This method allows for recovery of (1) cash-related pro forma operating expenses; (2) recovery of depreciation expense, a non-cash item, to provide working capital;<sup>44</sup> (3) the average annual principal and interest payments on all long-term debts, and (4) working capital that is in addition to depreciation expense.

	<u>Buffalo Trail Water Association</u>	<u>Staff</u>	
Pro Forma Operating Expenses	\$ 624,601	\$ 773,593	
Plus: Avg. Annual Principal and Interest Payments	57,303	57,303	(1)
Debt Coverage Requirement	<u>11,461</u>	<u>11,461</u>	(2)
Overall Revenue Requirement	693,365	842,357	
Less: Other Operating Revenue	57,856	(4,628)	
Miscellaneous Service Revenue	19,650		
Interest Income	<u>9,074</u>	<u>(9,074)</u>	
Revenue Required From Water Sales	779,945	828,655	
Revenue from Sales at Present Rates	<u>(734,299)</u>	<u>\$ (734,218)</u>	
Required Revenue Increase	<u><u>45,646</u></u>	<u><u>94,437</u></u>	
Percentage Increase	6.22%	12.86%	

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<sup>44</sup> The Kentucky Supreme Court has held that the Commission must permit a water district to recover its depreciation expense through its rates for service to provide internal funds for renewing and replacing assets. See *Public Serv. Comm'n of Kentucky v. Dewitt Water Dist.*, 720 S.W.2d 725, 728 (Ky. 1986). Although a water district's lenders require that a small portion of the depreciation funds be deposited annually into a debt reserve/depreciation fund until the account's balance accumulates to a required threshold, neither the Commission nor the Court requires that revenues collected for depreciation be accounted for separately from the water district's general funds or that depreciation funds be used only for asset renewal and replacement. The Commission has recognized that the working capital provided through recovery of depreciation expense may be used for purposes other than renewal and replacement of assets. See Case No. 2012-00309, *Application of Southern Water and Sewer District for an Adjustment in Rates Pursuant to the Alternative Rate Filing Procedure for Small Utilities* (Ky. PSC Dec. 21, 2012).

1. Average Annual Principal and Interest Payments. At the time of Staff's review, Buffalo Trail Water had three outstanding United States Department of Agriculture, Rural Development (USDA/RD) promissory notes. In its application, Buffalo Trail Water requested recovery of the average annual principal and interest on its indebtedness based on a five-year average of the annual principal, and interest and fee payments for the years 2022 through 2026.<sup>45</sup> Staff agrees with the methodology Buffalo Trail Water proposes. As shown below, Staff calculated an Average Principal and Interest Payment of \$57,303

Annual Principal and Interest Payment				
Year	Note 91-06 <sup>46</sup>	Note 91-08 <sup>47</sup>	Note 91-10 <sup>48</sup>	Total
2022	20,400	19,440	17,463	\$57,303
2023	20,400	19,440	17,463	57,303
2024	20,400	19,440	17,463	57,303
2025	20,400	19,440	17,463	57,303
2026	20,400	19,440	17,463	57,303
Totals	102,000	97,200	87,315	286,515
Divide by: 5 years				5
Average Annual Interest Payment				<u>57,303</u>

2. Additional Working Capital. The DSC method, as historically applied by the Commission, includes an allowance for additional working capital that is equal to the

<sup>45</sup> Application, 2020RDstatement.pdf.

<sup>46</sup> Case 1998-355, *Application of Buffalo Trail Water Association, Inc. of Sardis, Kentucky, for (1) A Certificate of Public Convenience and Necessity; (2) Approval of the Proposed Plan of Financing Said Project*, (Ky. PSC July 31, 1998).

<sup>47</sup> Case 2003-00128, *Extensions, Storage Tank*, (Ky. PSC May 6, 2003).

<sup>48</sup> Case 2017-00193, *Application of Buffalo Trail Water Association, Inc. for a Certificate of Public Convenience and Necessity to Construct and Finance Pursuant To KRS 278.023*, (Ky. PSC June 12, 2017).

minimum net revenues required by a district's lenders that are above its average annual debt payments. In the application, Buffalo Trail Water requested recovery of an allowance for working capital that is equal to 110 percent of its average annual debt payments for its bonds payable to the USDA/RD, the Kentucky Infrastructure Authority, and Kentucky Rural Water Finance Corporation at the time of its application. In response to Staff's Second Request, Buffalo Trail Water filed an updated revenue required calculation,<sup>49</sup> and in this calculation Buffalo Trail Water used 120 percent to calculate the Additional Working Capital.

USDA/RD requires that Buffalo Trail Water charge rates that produce net revenues that are at least 120 percent of its average annual debt payments. Following the Commission's historic practice, Staff agrees with Buffalo Trail Water's revised methodology. Therefore, \$11,461 is included it in the revenue requirement.

Average Annual Principal and Interest	\$	57,303
Times: DSC Coverage Ratio		<u>120%</u>
Total Net Revenues Required		68,764
Less: Average Annual Principal and Interest		<u>(57,303)</u>
Additional Working Capital	\$	<u><u>11,461</u></u>

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<sup>49</sup> Buffalo Trail Water's Response to Staff's Second Request, Item 9, Updated Revenue Required Calculations.

Signatures

          /s/ William M. Foley          

Prepared by: William Foley  
Revenue Requirements Branch  
Division of Financial Analysis

          /s/ Sam Reid          

Prepared by: Sam Reid  
Rate Design Branch  
Division of Financial Analysis

          /s/ Liz Stefanski          

Prepared by: Liz Stefanski  
Rate Design Branch  
Division of Financial Analysis

APPENDIX

APPENDIX TO A STAFF REPORT OF THE KENTUCKY PUBLIC SERVICE COMMISSION IN CASE NO. 2021-00205 DATED SEP 10 2021

Monthly Water Rates

5/8- x 3/4-Inch Meter

First 1,000 Gallons	\$ 17.43 Minimum Bill
Next 4,000 Gallons	0.00778 Per gallon
Next 5,000 Gallons	0.00575 Per gallon
Over 10,000 Gallons	0.00524 Per gallon

3/4-Inch Meter

First 5,000 Gallons	\$ 48.53 Minimum Bill
Next 5,000 Gallons	0.00575 Per gallon
Over 10,000 Gallons	0.00524 Per gallon

1-Inch Meter

First 10,000 Gallons	\$ 77.26 Minimum Bill
Over 10,000 Gallons	0.00524 Per gallon

1 1/2-Inch Meter

First 15,000 Gallons	\$ 103.44 Minimum Bill
Over 15,000 Gallons	0.00524 Per gallon

2-Inch Meter

First 20,000 Gallons	\$ 129.62 Minimum Bill
Over 20,000 Gallons	0.00524 Per gallon

4-Inch Meter

First 40,000 Gallons	\$ 252.30 Minimum Bill
Over 40,000 Gallons	0.00524 Per gallon

Wholesale Rates

Mt. Olivet Water Company	0.00304 Per gallon
Nicholas County Water District	0.00372 Per gallon

Nonrecurring Charges

Meter Connection/Tap-On Charge	\$1,176.00
Meter Turn-On Charge	16.80
Meter Test Charge	74.80
Meter Re-read Charge	16.80
Service Call/ Investigation Charge	16.80
Service Reconnection Charge	21.00
Returned Check Charge	9.00
Lock Removal	22.00

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